

# **CALIFORNIA LOTTERY**

Audit Report

## **CASANOVA PENDRILL PUBLICIDAD, INC. CONTRACT**

*January 1, 2008, through April 30, 2011*



**JOHN CHIANG**  
California State Controller

April 2012



**JOHN CHIANG**  
**California State Controller**

April 2, 2012

California Lottery Commission  
700 North Tenth Street  
Sacramento, CA 95811

Dear Commissioners:

The State Controller's Office audited the California Lottery's (Lottery) contract with Casanova Pendrill Publicidad, Inc. (contractor), Contract No. 10050, for the period of January 1, 2008, through April 30, 2011.

The purpose of the audit was to determine whether the Lottery's fiscal controls over payments are adequate and whether the Lottery's monitoring procedures are adequate to ensure that the contractor complies with the terms and conditions of the contract.

Our audit disclosed the following deficiencies:

- The Lottery did not comply with the Contract Verification Memos section of the Lottery Contract Manager's Handbook. We noted that the Lottery did not perform quarterly contract payment reconciliations for the two quarters ended June 30, 2009, and September 30, 2009.
- The Lottery did not properly monitor the Production Prop Policy of the contract. The Lottery lacked evidence to support that the contractor distributed \$3,100 of props and wardrobe, consisting of multiple items with retail values of less than \$1,000, to a non-profit organization.

If you have any questions, please call Andrew Finlayson, Chief, State Agency Audits Bureau, at (916) 324-6310.

Sincerely,

*Original signed by*

**JEFFREY V. BROWNFIELD**  
Chief, Division of Audits

JVB/vb

cc: Nathaniel Kirtman III, Commissioner  
California Lottery Commission  
John Smolin, Commissioner  
California Lottery Commission  
Phil Tagami, Commissioner  
California Lottery Commission  
Robert T. O'Neill, Director  
California Lottery  
Mike Ota, Deputy Director, Finance  
California Lottery  
Roberto Zavala, Chief Internal Auditor  
California Lottery

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# Audit Report

## Summary

The State Controller's Office (SCO) audited the California Lottery's (Lottery) contract with Casanova Pendrill Publicidad, Inc. (contractor), Contract No. 10050, for the period of January 1, 2008, through April 30, 2011.

The purpose of the audit was to determine whether the Lottery's fiscal controls over payments are adequate and whether the Lottery's monitoring procedures are adequate to ensure that the contractor complies with the terms and conditions of the contract.

Our audit disclosed the following deficiencies:

- The Lottery did not comply with the Contract Verification Memos section of the Lottery Contract Manager's Handbook. We noted that the Lottery did not perform quarterly contract payment reconciliations for the two quarters ended June 30, 2009, and September 30, 2009.
- The Lottery did not properly monitor the Production Prop Policy of the contract. The Lottery lacked evidence to support that the contractor distributed \$3,100 of props and wardrobe—consisting of multiple items with retail values of less than \$1,000—to a non-profit organization.

## Background

By authority of the California Constitution, Government Code section 12410 states, "The Controller shall superintend the fiscal concerns of the state. The Controller shall audit all claims against the state, and may audit the disbursement of any state money, for correctness, legality, and for sufficient provision of law for payment." In addition, Government Code section 12411 stipulates that "... the Controller shall suggest plans for the improvement and management of revenues."

Proposition 37, the California State Lottery Act of 1984 (Lottery Act), amended the California Constitution to authorize the establishment of a statewide lottery, to create the California Lottery Commission, and to give the commission broad powers to oversee the operation of a statewide lottery.

Pursuant to Government Code section 8880.67, the SCO may conduct other special post-audits of the Lottery, as the State Controller deems necessary. The Controller or his or her agents conducting an audit under this chapter shall have access and authority to examine any and all records of the California Lottery Commission.

The Lottery entered into a contract with Casanova Pendrill Publicidad Inc., Contract No. 10050, to provide Hispanic-market advertising services for all Lottery products. The original contract period was June 1, 2005, through May 31, 2009, with an option to renew up to two years,

for a maximum amount of \$28,000,000. Amendment A01 amended Exhibit B, Section 1.7, Loss Prevention. Amendment A02, approved on April 24, 2009, extended the term to May 31, 2011, and increased the maximum amount by \$12,000,000. Amendment A03, approved on December 22, 2010, extended the term to December 31, 2011, and increased the maximum amount by \$6,000,000 to a total of \$46,000,000.

The contractor agreed to provide the following services:

- Assist in overall marketing analysis, strategy development, and positioning of the California Lottery and its products.
- Share responsibility for planning, coordinating, and executing specific portions of the Lottery's annual advertising plan.
- Create and produce Hispanic-market (Spanish-language) advertising customized for the Lottery's existing products and new products.
- Advise with respect to creative and talent matters relating to broadcast production, as necessary:
  - Provide Spanish-language translation services.
  - Develop Hispanic-market media plans and purchase Spanish-language television, radio, print, outdoor, and any new media vehicles.
  - The Lottery may request the contractor to develop, design, and provide in-store communications and components.

The purpose of the audit was to determine whether the Lottery's fiscal controls over payments and monitoring procedures are adequate to ensure that the contractor complies with the terms and conditions of the Casanova Pendrill Publicidad, Inc., Contract No. 10050.

## **Objectives, Scope, and Methodology**

We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We did not audit the Lottery's financial statements. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

The specific audit objectives were to determine whether the Lottery is:

- Ensuring that contract payments are legal and proper;
- Abiding with state laws, rules, regulations, and policies with regard to the contract;
- Monitoring the contract for compliance; and
- Ensuring that the contractor provides the Lottery with specified deliverables according to the terms and conditions of the contract.

The audit period was January 1, 2008, through April 30, 2011, and included, but was not limited to, the following audit procedures:

- Reviewing work performed by any external audit organization or by any other Lottery unit;
- Interviewing and observing individuals involved in the development, authorization, and monitoring of the contract;
- Performing tests of procedural compliance and tests of payments, as we deemed necessary; and
- Obtaining an understanding of components of internal controls sufficient to conduct the audit.

## **Conclusion**

Our audit disclosed that the Lottery did not follow the terms and conditions stipulated in the Casanova Pendrill Publicidad, Inc. contract and the Lottery Contract Manager's Handbook. We noted the following deficiencies:

- The Lottery did not comply with the Contract Verification Memos section of the Lottery Contract Manager's Handbook. We noted that the Lottery did not perform quarterly contract payment reconciliations for the two quarters ended June 30, 2009, and September 30, 2009.
- The Lottery did not properly monitor the Production Prop Policy of the contract. There was no evidence to support that the contractor distributed \$3,100 of props and wardrobe, consisting of multiple items with retail values of less than \$1,000, to a non-profit organization.

## **Views of Responsible Official**

We issued a draft report to the Lottery dated February 10, 2012. Robert O'Neill, Director, responded by the attached letter dated March 1, 2012. Mr. O'Neill agreed with the findings and recommendations.

## **Restricted Use**

This report is intended for the information and use of the California Lottery, the California Lottery Commission, and the SCO; it is not intended to be and should not be used by anyone other than these specified parties. This restriction is not intended to limit distribution of the final report, which is a matter of public record.

*Original signed by*

JEFFREY V. BROWNFIELD  
Chief, Division of Audits

April 2, 2012

# Findings and Recommendations

## **FINDING 1— Lack of contract payment reconciliation**

The California Lottery (Lottery) did not consistently perform quarterly contract payment reconciliations between the Lottery contract manager's payment logs and the official accounting records. We noted the following deficiencies:

- The accounting office failed to send contract balance verification memos to the manager of the Casanova Pendrill Publicidad, Inc. contract for the two quarters ended June 30, 2009, and September 30, 2009.
- The contract manager failed to perform payment reconciliations for the two quarters ended June 30, 2009, and September 30, 2009.

The Lottery Contract Manager's Handbook, Chapter 4, page 16, states the following:

The accounting office sends a contract verification memo to the contract manager the first week of every quarter. The memo must be reviewed and approved, and returned to the accounting office approximately two weeks from the date of the memo. This ensures that the available balance for the contract was the same on both the contract manager's and accounting office's payment logs. This also ensures that the contract manager has seen all invoices paid against the contract and helps to verify that accounting has received and paid all invoices that the contract manager has approved.

If the Lottery does not consistently reconcile the contract manager's available balance to the accounting office's payment logs, the following may occur:

- An invoice may be paid without the contract manager's approval.
- An invoice approved by the contract manager may not be paid.
- The contract payments could exceed the contract's available balance.

### Recommendation

The Lottery's accounting office should send contract balance verification memos to the contract manager every quarter to ensure that payment reconciliations are consistently performed.

The contract manager should implement controls to ensure that he or she consistently performs quarterly payment reconciliations.

### Lottery's Response

The Lottery agrees with the finding and recommendation. During the two quarters in question, a staff vacancy in the Lottery's Finance Division caused a variation to normal operation. While reconciliations were temporarily deferred to manage the workload, designated back-up staff continued to process Casanova invoices for payment in accordance with the California Prompt Payment Act. All invoices during this time period were properly approved and supported.



During this period, the Contract Manager's staff continued to review, verify and log invoices against a quarterly budget balance. As noted, the Contract Manager also reviewed and approved each invoice for completeness and accuracy. After the third quarter of 2009, the Contract Manager's payment reconciliations resumed with no discrepancies. During this time the contract's available balance was not exceeded.

To mitigate the risk of not properly approving, not paying invoices and exceeding contract balances, the Lottery's Finance Division has since put a process in place to ensure contract balance verification memos are sent to contract managers quarterly and payment reconciliations are consistently completed every quarter.

#### SCO's Comment

The California Lottery concurs with the finding and is implementing an additional process to ensure that payment reconciliations are consistently completed every quarter. We will follow up on the Lottery's corrective actions at a later date to determine whether they were properly implemented.

#### **FINDING 2— Inadequate monitoring of Production Prop Policy**

The Lottery lacked adequate evidence to support that it properly monitored the Production Prop Policy of the contract terms. We noted the following deficiency in the Lottery's monitoring procedures of the contract:

According to the Film Production Cost Summary and the related invoice, the Lottery purchased \$3,100 worth of props and wardrobe, consisting of multiple items with retail values of less than \$1,000. The Production Prop Policy of the contract, Exhibit F, states that props purchased and having retail value of \$1,000 or less, which cannot be sold, shall be distributed to an appropriate non-profit or charity organization. The Lottery lacked evidence to support that the contractor distributed the multiple items valued at a total of \$3,100 to a non-profit or charity organization, as required by the contract.

The Production Prop Policy of the contract, Exhibit F, states the following:

The Lottery, through contracted or subcontracted advertising agencies, may purchase props to be used in production of print and television advertising and special events. The purpose of this policy is to outline the procedure to be followed for disposing of props used in the production of commercials of special events for the Lottery. This policy pertains to any and all props (including wardrobe, furniture, household supplies, etc.) built, rented or purchased for the Lottery.

Written into each original contract between the contractor and a production house will be a clause stating that within thirty days of the completion of production, all props shall be turned over to the contractor. The contractor shall return or distribute props according to the following:

Props, which were rented, shall be returned to the rental company. If a credit is due, the contractor shall receive the monies and shall credit the Lottery on the following month's billing for money received.

Props, which were purchased and have a retail value at \$1,000 or more, are the property of the Lottery. Props with a retail value at \$1,000 or less, which cannot be sold, shall be distributed to an appropriate non-profit or charity organization. Props with a retail value at more than \$1,000 shall be returned to the Lottery at the end of each quarter, along with a list of the items being returned and which production the items appeared in. The contractor shall notify the Lottery prior to shipping the items to the Lottery. Contractor may submit an estimate to the Lottery to cover the cost of shipping the items to the Lottery. Upon receipt, the Lottery shall determine how the items will be disbursed.

If the Lottery does not monitor the Production Prop Policy, the following may occur:

- Moneys (credits) received from rental companies may not be credited to the Lottery.
- Props that are purchased and have a retail value of less than \$1,000 might not be properly distributed to a non-profit or charitable organization.
- Props that are purchased and have a retail value of \$1,000 or more, and are considered property of the Lottery, might not be returned to the Lottery.

#### Recommendation

The Lottery should implement controls that will monitor the contract's Production Prop Policy to ensure that the contractor properly disposes of props used in the production of commercials or special events.

#### Lottery's Response

The Lottery agrees with the finding and recommendation and will ensure that any future production prop and/or wardrobe disposals are in accordance with contract requirements. Further, the Lottery will be reviewing industry best practices to assist in the development and implementation of controls to monitor the updated policy regarding props.

#### SCO's Comment

The California Lottery concurs with the finding and will develop and implement controls to monitor the updated policy regarding props. We will follow-up on the Lottery's corrective actions at a later date to determine whether they have been properly implemented.

**Attachment—  
California Lottery's  
Response to Draft Report**

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700 North Tenth Street  
Sacramento, CA 95811  
[calottery.com](http://calottery.com)



March 1, 2012

Jeffrey V. Brownfield, Chief  
Division of Audits  
State Controller's Office  
Post Office Box 942850  
Sacramento, California 94250-5874

Re: Casanova Pendrill Publicidad, Inc. Contract No. 10050

Dear Mr. Brownfield:

The California Lottery (Lottery) offers the following general comments and specific points regarding the recently concluded audit conducted by the State Controller's Office (SCO). The audit scope was limited to an audit of the Lottery's fiscal control over payments and monitoring procedures in Casanova Pendrill Publicidad, Inc. (Casanova) Contract No. 10050.

The Lottery takes its mission as a public agency very seriously. We recognize that it is an important part of this mission to perform its duties in a cost-effective and transparent manner to ensure that there has been no violation of the public trust. As noted, the focus of the audit was on the fiscal control over payments and monitoring procedures and we are pleased to note that in this area, after a lengthy and thorough review by the SCO, there are no findings that would hinder the Lottery's performance of its mission.

The draft report listed recommendations for the Lottery to consider. These recommendations call for the Lottery to be in compliance with the Contract Manager's Handbook by conducting timely quarterly reconciliations and ensuring that proper disposals follow contract requirements. The Lottery continually evaluates and implements methods to improve its business practices and refine its internal control structure, and intends to adopt these recommendations that cost effectively improve business functions.

Below are the Lottery's responses to the specific recommendations provided in the draft audit report. The Lottery will develop a work plan as part of the SCO follow-up process.

**FINDING 1 – Lack of contract payment reconciliation**

The Lottery did not consistently perform quarterly reconciliations between the Lottery contract manager's payment log and the official accounting records. We noted the following deficiencies:

1. The accounting office failed to send contract balance verification memos to the manager of the Casanova contract for the two quarters ended June 30, 2009, and September 30, 2009.
2. The Casanova contract manager failed to perform payment reconciliations for the two quarters ended June 30, 2009, and September 30, 2009.

**RECOMMENDATION:**

The Lottery's accounting office should send contract balance verification memos to the contract manager every quarter to ensure that payment reconciliations are consistently performed.

The contact manager should implement controls to ensure that he/she consistently performs quarterly payment reconciliations.

**RESPONSE:**

The Lottery agrees with the finding and recommendation. During the two quarters in question, a staff vacancy in the Lottery's Finance Division caused a variation to normal operations. While reconciliations were temporarily deferred to manage the workload, designated back-up staff continued to process Casanova invoices for payment in accordance with the California Prompt Payment Act. All invoices during this time period were properly approved and supported.

During this period, the Contract Manager's staff continued to review, verify and log invoices against a quarterly budget balance. As noted, the Contract Manager also reviewed and approved each invoice for completeness and accuracy. After the third quarter of 2009, the Contract Manager's payment reconciliations resumed with no discrepancies. During this time the contract's available balance was not exceeded.

To mitigate the risk of not properly approving, not paying invoices and exceeding contract balances, the Lottery's Finance Division has since put a process in place to ensure contract balance verification memos are sent to contract managers quarterly and payment reconciliations are consistently completed every quarter.

Jeffrey V. Brownfield  
March 1, 2012  
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**FINDING 2 – Inadequate Monitoring of the Production Prop Policy**

The Lottery did not properly monitor Production Prop Policy of the contract. The Lottery lacked evidence to support that the contractor distributed \$3,100 of props and wardrobe, consisting of multiple items having retail values of less than \$1,000, to a non-profit organization.

**RECOMMENDATION:**

The Lottery should implement controls that will monitor the contract's Production Prop Policy to ensure that the contractor properly disposes of props used in the production of commercials or special events.

**RESPONSE:**

The Lottery agrees with the finding and recommendation and will ensure that any future production prop and/or wardrobe disposals are in accordance with contract requirements. Further, the Lottery will be reviewing industry best practices to assist in the development and implementation of controls to monitor the updated policy regarding props.

If you have any additional questions, please contact my Audit Chief, Roberto Zavala at (916) 822-8358.

Sincerely,

A handwritten signature in blue ink, appearing to read "R. T. O'Neill", is written over a light blue horizontal line.

Robert T. O'Neill  
Director

**State Controller's Office  
Division of Audits  
Post Office Box 942850  
Sacramento, CA 94250-5874**

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